traditional depreciation represcription process has again resulted in inadequate depreciation rates for LECs, and a significant depreciation reserve deficiency. It is imperative that the Commission now adopt long-overdue reform of the depreciation represcription process in this proceeding. Such reform must provide carriers with the flexibility to establish depreciation rates that are consistent with the actual remaining lives of depreciable assets.

E. <u>A simplified depreciation prescription process must include flexibility for carriers to reflect technological obsolescence</u>.

Evidence of the rapidly changing, increasingly competitive telecommunications marketplace occurs every day in the headlines:

*AT&T Reenters Local Market: Acquires McCaw Cellular

*Time Warner Announces Two-Way Video in Orlando

*Cox Purchases Majority Interest in Teleport

*SW Bell Acquires Cable TV Companies Outside D.C.

*SW Bell, Cox Announce U.K. Cable Joint Venture

*Peter Huber Describes Geodesic Network

*FCC Requires Expanded Interconnection/Collocation

*FCC Unbundles Access: Local Transport Competitive

*Ameritech Proposes New Regulatory Model: Will Swap Unbundled Access for InterLATA Authority

*Pac Tel to Restructure: Spin-off Cellular Properties

*Rochester Tel Denounces Franchise for Full Competition

*Ameritech/US West to Deploy Broadband Fiber Networks

As these fundamental changes unfold, depreciation flexibility is needed to treat price cap LECs equitably with their principal competitors. AT&T has been allowed almost double the regulated depreciation rate prescribed for BellSouth. Non-dominant interexchange carriers' depreciation rates are not regulated by the Commission. Nor are the depreciation rates of cable television companies. As a result, cable television companies have adopted depreciation rates almost double those of the price cap LECs. The following chart compares 1991 depreciation rates of cable television companies, interexchange carriers, GTE and the Bell operating companies.

TELECOMMUNICATIONS INDUSTRY

1991 Depreciation Rate Comparison

Carrier	FR Rate*	MR Rate**
Cable TV	13.9%	N/A
AT&T	9.9%	13.8%
Sprint	8.5%	N/A
MCI	8.1%	N/A
BellSouth	7.9%	7.0%
GTE	7.7%	6.5%
NYNEX	7.6%	7.0%
Ameritech	7.2%	6.9%
Pac Tel	7.0%	6.8%
Bell Atlantic	7.0%	6.6%
SW Bell	7.0%	6.0%
US West	6.8%	6.3%

*FR Corporate rates are from Compustat Database
** MR rates are composite of regulated subsidiaries from Form M.

To the extent that past Commission practices have deferred recovery of capital to the future, the ability of this Commission and state regulators to insure actual recovery of that capital is tenuous at best. BellSouth urges the Commission to act decisively in this proceeding to make meaningful depreciation reform.

II. BellSouth supports the Price Cap Carrier Option for the interstate services of price cap LECs.

Of the four options set forth in the NPRM, only the Price Cap Carrier Option ("PCCO") is consistent with the responsibility assumed by price cap carriers and with the incentive structure that price cap regulation was designed to promote. In treating depreciation rates as endogenous under price cap regulation, the Commission stated:

> Specifically, the idea behind price caps is to provide carriers with the proper incentives toward efficiency and productivity. Since a carrier's decision about how and when to deploy new plant is fundamental to these objectives, if we were to guarantee depreciation expense, we would distort the carrier's business process. That is, we believe that carriers should decide to replace plant when it is economically prudent to do so, and should not base this decision on depreciation accounting. If carriers are required to live with the depreciation rates that result from their investment decisions, we believe that we can reasonably assume that they will make decisions that will enhance productivity in the long run.[29]

Although the Commission placed the economic consequences of capital recovery decisions squarely on the price cap carriers, the Commission withheld one of the essential tools needed by the carriers to achieve capital recovery: control over their depreciation rates. The

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[29] In the Matter of Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Second Report and Order, FCC No. 90-314, released October 4, 1990, para. 183.

Commission stated:

> While it may be true, as some LECs contend, that technological obsolescence due to consumer expectations and demand is reducing the "useful life" of their assets much faster than physical obsolescence, determining the most appropriate standard for calculating depreciation rates is beyond the scope of this proceeding.[30]

In essence, the Commission's policy decisions gave price cap carriers a three-legged stool to effectuate capital recovery, but with one of the legs sawed off by the Commission. Although carriers make the decisions on when to deploy and retire plant (two legs of the stool), inaccurate Commission estimates of the remaining useful life of those assets, and hence inadequate depreciation rates (the third leg), impede the efforts of the LECs to achieve full capital recovery. Price cap LECs have found a two-legged stool to be very unstable. The Commission should provide the third leg of the stool in this proceeding.

As the studies cited earlier in these comments make clear, inadequate capital recovery burdens not only carriers and their shareowners, but also society as a whole. It hampers badly needed infrastructure development, tips the competitive playing field, and distorts reported earnings of effected carriers.

The PCCO, as modified below, places the responsibility for adequate capital recovery squarely on the parties bearing the risk of nonrecovery--the price cap LECs and

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[30] Id., para. 184.

their shareowners. The PCCO can be implemented in a way the satisfies the Commission's need for information and allows the Commission to fulfill its responsibilities under the Communications Act.

In paragraph 41 of the NPRM, the Commission states:

> Under this proposal, carriers would seek depreciation rate changes by filing with this Commission the following information: their depreciation rates in effect, their proposed depreciation rates, and the changes in depreciation expense that they would experience if the proposed rates became effective. Carriers would not be required to provide supporting data for their proposed depreciation rate changes. This option would essentially eliminate all of the steps the Commission now takes to analyze the carriers proposed depreciation rate changes.

The PCCO proposed in the NPRM goes farther than is necessary to provide price cap carriers with effective responsibility for their own depreciation rates. BellSouth suggests that the PCCO should give carriers primary responsibility for setting their own depreciation rates. However, the Commission must retain the controls necessary to meaningfully evaluate and, should it become necessary, to prescribe lives other than those proposed by the price cap carriers. For the Commission to have sufficient control over the depreciation represcription process, BellSouth suggests that the Commission could require that price cap carriers:

1) Determine depreciation accrual requirements by investment account, as is done today.

2) Use the same depreciation theory and methods that

are used today to determine depreciation expense requirements. Specifically, price cap carriers would continue to use "remaining life" procedures, including the Depreciation Reserve Ratio, to insure that no more than 100 percent of the investment is depreciated.[31] Price cap carriers would also continue to use the "equal life group" methodology, which matches capital recovery more closely with capital consumption.

3) File with the Commission the depreciation rates in effect, the proposed rates, and the change in accrual expense that would occur if the new rates are permitted to take effect. Carriers should be required to file no less often than every three years, but carriers must have an option to file annually. BellSouth will provide the remaining lives, salvage and reserve levels of every account that is used in the calculation of the proposed rate and the accrual changes that will result from application of the new rate, as is current practice, to provide the Commission and interested parties with the information necessary to evaluate the proposed depreciation rates.

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[31] A decade ago, Former Commissioner Fogarty concluded that this was the only regulatory control necessary. "The only control over the process that the commission need exercise is to assure that no more than 100 per cent of costs are recovered. The marketplace with its competitive pricing constraints are the threat of bypass should be an adequate regulator of the timing of depreciation recoveries." Fogarty, "Capital Recovery: A Crisis for Telephone Companies, a Dilemma for Regulators", Public Utility Fortnightly, December 8, 1983, p. 17.

4) Certify that the depreciation rates utilized were developed in compliance with Part 32 of the Commission's Rules and with Generally Accepted Accounting Principles ("GAAP").

The Commission would then place the carrier filing on Public Notice. State Commissions and the public would be invited to comment on the carrier's proposal. The carriers would respond to any questions raised by commenting parties or the Commission staff regarding the proposal, but would not be required to produce underlying study documents as is done today. Following the comment cycle, the Commission would prescribe the depreciation rates proposed by the percentages of depreciation which shall be charged with respect to each such class of property. Depreciation charges would be applied to the existing classes of property under the uniform system of accounts. Depreciation rates would continue to be prescribed by the Commission for each such class of property. The only change would be in the amount and type of data submitted to the Commission and in the weight to be accorded to the views of carrier management regarding the future remaining lives of the carrier's depreciable assets.

The proposed procedures will also satisfy the Commission's obligation under Section 220(i) of the Communications Act with regard to state commissions with jurisdiction over the intrastate operations of the carriers. Notice and Comment procedures are sufficient to satisfy the Commission's obligation under Section 220(i) of the Communications Act to notify state commissions having intrastate jurisdiction with respect to the filing carrier, to give reasonable opportunity to each such commission to present its views, and to consider such views and recommendations. The Commission has consistently used Notice and Comment procedures to fulfill the comparable requirements of Section 221(a) of the Communications Act when reviewing applications for consolidations and mergers of telephone companies. As additional assurance that the state commissions receive actual rather than constructive notice, the Commission could require that each price cap carrier filing for revised depreciation rates serve a copy of the filing on each state commission having jurisdiction over the intrastate operations of that carrier.

If adopted, the process described above will insure reasonable depreciation rates for the interstate operations of price cap carriers. There will be ample safeguards to insure that the PCCO operates in the public interest and protects ratepayers from unreasonable rates.

IV. The Price Cap Carrier Option provides ample protection for ratepayers.

Ratepayer interests will be amply protected under the PCCO, as modified above. A series of effective consumer protections will remain in place that will prevent abuse of the depreciation represcription process under the PCCO.

A. Carriers utilizing the PCCO will continue to use ELG and "remaining life" in setting their depreciation rates.

As noted above, the continued use of "remaining life" and ELG will insure that carriers will recover no more than 100 percent of their original investment.

B. Carriers will be subject to GAAP requirements in determining depreciation rates under the PCCO.

Carriers will follow GAAP to determine depreciation rates. GAAP accounting provides a significant safeguard for ratepayers. Depreciation results in periodic recognition of the consumption of an asset. The original cost of an asset is allocated (charged to expense) systematically and rationally over its useful life.[32] In order to comply with GAAP, carriers are required to match costs to the benefitted period (the matching principle), and to consistently apply accounting principles and concepts from period to period (the consistency principle).

1. The Matching Principle.

GAAP requires that companies match costs to the period in which revenues produced by those costs are earned. Since depreciable assets benefit more than one accounting period, compliance with the matching principle requires the cost of assets be allocated to the benefitted periods. Depreciation expense represents the portion of asset cost allocated to the current accounting period.

Statement of Financial Concepts No. 5, Recognition and Measurement in Financial Statements of Business Enterprises, states, at paragraph 86:

> Some expenses, such as depreciation and insurance, are allocated by systematic and rational procedures to the periods during which the related assets are expected to provide benefits.

Thus, a carrier that attempted to manipulate its depreciation expense would violate the matching principle, and hence GAAP. As shown below, such a violation would be readily detectible and correctable.

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[32]AICPA, Accounting Research Bulletin No. 43: Restatement and Revision of Accounting Research Bulletins (June 1953), Chapter 9, Section 5.

2. <u>The Consistency Principle</u>.

The Accounting Principles Board ("APB"), predecessor to the Financial Accounting Standards Board addressed the requirement for consistency in applying accounting principles. APB Opinion No. 20, at paragraph 15, states in pertinent part:

> [I]n the preparation of financial statements there is a presumption that an accounting principle once adopted should not be changed in accounting for events and circumstances of a similar type.

The standard form for an auditor's report states that financial statements have been prepared "in conformity with generally accepted accounting principles <u>consistently applied</u>." Thus, an audit of carrier financial statements will include the necessary review to insure that the consistency principle has been followed.

3. <u>Straight line depreciation</u>.

Part 32 of the Commission's Rules incorporates GAAP. LECs are required by Section 32.2000(g) of the Rules to base depreciation on the straight-line methodology. Section 32.2000(g)(2)(ii) states, in pertinent part:

> Companies . . . shall apply such depreciation rate . . . as will ratably distribute on a straight line basis the difference between the net book cost of a class or subclass of plant and its estimated net salvage during the known or estimated remaining service life of the plant.

Section 32.2000(g)(2)(iv) of the Rules requires that carriers obtain prior Commission approval to amortize a depreciation reserve deficiency. Thus, the Commission's existing rules require that carriers follow GAAP accounting for depreciation, and that the Commission receive notice and approve any amortization of a reserve deficiency undertaken by a carrier. Absent such approval, any difference in depreciation rates would result from a change in the estimated remaining life for the equal life vintage groups. These rules provide an effective safeguard against any manipulation of depreciation rates by a carrier subject to Part 32 of the Rules.

C. <u>Existing reporting requirements will expose any attempt to manipulate depreciation rates</u>.

If the PCCO is adopted, the Commission will retain extensive reporting requirements that will make any attempt to manipulate depreciation rates apparent. For example, the ARMIS system results in depreciation reporting in both annual and quarterly reports.

Depreciation expense, allocated in accordance with Parts 36 and 69 and grouped by access elements, can be tracked quarterly on the ARMIS Report 43-01. The annual ARMIS Report 43-04 contains detailed, separated depreciation expenses and reserves by plant summary accounts. In addition, the revised ARMIS Report 43-02 will contain extensive, mechanized data on depreciation previously reported in FCC Form M. The Commission is also proposing to include the ARMIS Report 43-02 an annual data request on depreciation.

The annual USOA Report, ARMIS Report 43-03, provides detailed information that is audited by independent auditors to insure compliance with the joint cost order rules. The Commission requires that the independent auditors certify that the ARMIS Report 43-03 "fairly presents" the financial status of the carrier. Even as modified under the PCCO, the Commission will have no difficulty identifying any attempt by a carrier to manipulate its depreciation rates.

D. <u>The "sharing" feature of the LEC price cap plan will not result in manipulation of depreciation rates under the PCCO</u>.

Paragraph 40 of the NPRM raises the issue of the effect of the sharing provision of the LEC price cap plan on carrier depreciation decisions. Specifically, the NPRM poses the following question:

> We note that under the LEC price cap scheme, LECs must share earnings with their customers if earnings fall within a specified sharing zone. We seek comment on whether the sharing mechanism will have any impact on LEC depreciation decisions.

Commissioner Ervin Duggan, in his Concurring Statement, amplified the concerns underlying this question:

> Even for carriers under price caps, prescribing accurate depreciation rates is essential. Changes in depreciation expense may not directly affect the price cap index, but such expenses can affect the price cap indirectly if the carriers are earning enough to be in the sharing zone, where they are obliged to share excess earnings with ratepayers through future reductions in the price caps. Carriers thus have the incentive even under price caps to manipulate depreciation expenses in order to avoid the sharing obligation. The sharing mechanism, in my judgment, is a key part of the consumer protections established under the price cap plan for local telephone companies--and should not be undermined.

BellSouth agrees with Commissioner Duggan that accurate depreciation is essential. The problem is that the present interstate depreciation represcription process has not resulted in accurate depreciation. For example, in the underground cable-metallic account, the FCC's currently prescribed average remaining life for Southern Bell is 14.1 years. The Florida Public Service Commission recently prescribed an average remaining life of 6.0 years for the same account. The discrepancy is primarily due to the FCC's emphasis on historical data, while the Florida commission has placed much more emphasis on the probability of technological obsolescence in this account.

The independent studies cited in the Introduction section of these Comments clearly demonstrate that the existing depreciation represcription process, with its overriding emphasis or mortality data, has resulted in inadequate regulated depreciation rates for the price cap LECs. As noted above, BellSouth currently has a depreciation reserve deficiency in excess of a $1.5 billion in the four major Metallic Cable and Circuit accounts. Thus, when BellSouth reports its regulated financial results to the Commission, its true earnings level is significantly overstated.

AT&T, the primary beneficiary of LEC "sharing" under price caps, recognizes the distortion that inadequate depreciation has on reported regulated financial results in its Petition for Waiver filed January 27, 1993.[33] At page 16 of its Petition, AT&T states:

> Understating AT&T's MR depreciation expenses could lead to an inaccurate presentation of AT&T's financial condition for regulatory purposes. For example, understated depreciation expenses may erroneously inflate AT&T's regulatory earnings level. The Commission has stated that its review of AT&T's performance of [sic] price caps will depend in part upon its assessment of AT&T's achieved rate of return during the review period. If the use of MR depreciation understates the appropriate depreciation expenses and thus overstates the achieved rate of return, the Commission's assessment of AT&T's performance would be based on distorted data and could lead to misguided regulatory decisions.

AT&T is correct when it notes that understated regulated depreciation expenses artificially inflate reported earnings. It is also correct that such discrepancies can prejudice the Commission's assessment of the effectiveness of price cap regulation. This prejudice is doubly damaging to the price cap LECs. Not only are apparent earnings inflated, leading to potential prejudice in the price cap review process, but the sharing mechanism results in the transfer to customers of what should be a return of investor capital.

As Commissioner Duggan correctly noted, during an initial "catch-up" period, while interstate depreciation reserves are being built up to proper levels, "sharing"

[33]See Public Notice, American Telephone and Telegraph Company Files Petition for Waiver of the Commission's Depreciation Methods and Procedures, DA 93-133, released February 11, 1993.

could be reduced. Given the existing depreciation reserve deficiency, this is entirely appropriate, not a sign of "manipulation" by the carrier. After this initial "catch-up" period, depreciation rates should stabilize, and possibly decrease as reserve levels are built up. Calculating a "sharing" obligation based on artificially inflated measures of income, as is the case today, is not sound regulatory policy. The Commission should not allow concerns about "sharing" to stand in the way of much needed reform of the depreciation prescription process.

Following each of the first two years of price cap regulation BellSouth has had a sharing obligation. During that same time, BellSouth has had a growing depreciation reserve deficiency that now totals more than $1.5 billion. Had BellSouth's depreciation expense been calculated based on reasonable remaining lives, much or all of that sharing obligation would have been properly classified by the Commission as a return of investor supplied capital, not net income. This would not have been the result of manipulation of depreciation rates, but simply an accurate reflection of the rate at which BellSouth's assets are being used to provide service to its customers.

As BellSouth has discussed above, the adoption of the PCCO for the interstate services of price cap LECs will result in an open represcription process in which all parties will be able to participate in a meaningful fashion.

The Commission retains the right and responsibility to investigate questionable filings. Any attempt to "manipulate" depreciation rates will be easily identifiable and subject to correction by the Commission. The "sharing" feature of the LEC price cap plan does not require rejection of the PCCO: indeed, it makes the adoption of the PCCO critically important, since the PCCO is most likely to result in accurate depreciation expenses.

E. Adoption of the PCCO will not hamper the Commission's ability to conduct a comprehensive review of price cap regulation.

In his Concurring Statement, Commissioner Ervin Duggan raises the issue of the effect adoption of the PCCO may have on the Commission's ability to monitor the progress of price cap regulation:

> Finally, the Commission needs accurate measures of depreciation expense so it can monitor the progress of price caps. If expenses are not accurately measured, it will become more difficult to assess the real level of telephone company earnings under price caps. Without accurate information, we will not be in a position to prescribe any necessary changes in the price cap formula at the time of the four-year price cap review.

BellSouth concurs with the view that an accurate measurement of depreciation expenses is critical to an objective review of price cap regulation. Unfortunately, as shown above, the level of depreciation expenses currently being recorded on the regulatory books is inadequate. Unless adjustments to regulated earnings are made to reflect the inadequacy of the existing depreciation rates, a distorted view of the success of price cap regulation will result, and will impair the Commission's ability to consider whether adjustments to the price cap plan are needed.

The comprehensive review of LEC price caps is scheduled to occur in 1994, based on 1991 through 1993 data. No changes are likely to result from the present rulemaking that would affect that data source. BellSouth assumes that if the PCCO option is adopted in this proceeding, its implementation would begin to effect the depreciation rates of price cap LECs in 1994. Therefore, adoption of the PCCO in this proceeding will not hamper the Commission's comprehensive review of LEC price caps.

V. BellSouth expresses secondary support for the Depreciation Rate Range Option and the Basic Factors Range Option.

BellSouth has shown above that the PCCO is the option that will best insure accurate depreciation rates for price cap carriers. Should the Commission be unwilling to adopt the PCCO, the Depreciation Rate Range Option ("DRRO") or the Basic Factors Range Option ("BFRO") could result in some administrative savings and somewhat more accurate depreciation rates.

Former FCC Commissioner Joseph Fogarty wrote in 1983:

> A depreciation rate is not a single figure. Instead, there is an appreciable zone of reasonableness within which the correct rate may

be expected to lie.[34]

The effectiveness of either the DRRO or the BFRO would depend on the incorporation of the following features:

1) The range of rates or factors must be wide enough to encompass changes in service lives of LEC assets resulting from the introduction of new technology and expanded competition. The range must, at a minimum, be wide enough to encompass existing prescribed depreciation rates. If the range is not sufficiently wide, there is a great risk that an individual carrier will suffer an increasing reserve

4) Computed Mortality Updates should be available for all accounts. This greatly reduces the amount of detailed information analysts must handle.

5) Carriers should be allowed, no more frequently than annually, to select a rate or factor within the range without having to run special or exception studies. If either option requires exception studies or the filing of full support data as previously required, that option will be of limited usefulness.

The Commission need not view with alarm the prospect of permitting carriers increased flexibility to determine their depreciation rates. There is evidence to suggest that such flexibility will not lead to abuse. In 1986, Ernst and Whinney conducted a "Review of Depreciation Policies and Procedures in Selected Industries" for the USTA. Ernst and Whinney surveyed sixteen companies in the airline, cable TV, computer manufacturing and electric utility industries to determine the factors that influence management decisions with regard to depreciation methods and procedures, depreciable lives, and the processes used to establish these methods and lives. The survey revealed the following significant findings:

--Fourteen of the sixteen companies used only straight line depreciation. Only computer manufacturers, which viewed the risk of technological obsolescence as the primary factor in setting depreciation rates, used accelerated depreciation methods.

--None of the companies used different depreciation methods for different business segments or locations.

--The unregulated companies do not have complicated processes or procedures to estimate the lives of depreciable assets. They establish depreciable lives on the basis of management judgments regarding the future economic usefulness of assets.

--The unregulated companies cite technological obsolescence most frequently as the factor which influences depreciation lives.

--All three nonregulated industries have informal processes for evaluating the reasonableness of depreciation lives.

--The nonregulated industries spend little time evaluating the cost of removal and salvage. Those companies who monitor gains and losses on disposal of assets report only small gains or losses.

--Generally, the companies surveyed devote less than the equivalent of one person year per year at the middle management level to evaluate depreciation.

While BellSouth does not advocate that the Commission permit price cap carriers to emulate the depreciation practices of unregulated companies, this survey should lead the Commission to conclude that accurate depreciation rates can be derived with far less emphasis on historic data, thereby placing more emphasis on the future economic usefulness of assets. The Commission can significantly reduce its reliance on historical data, and instead rely upon GAAP to insure that depreciation is rational, reasonable and consistent.

Of the two range options, BellSouth favors the DRRO. Other than the PCCO, the DRRO will save the greatest amount of time and money.[35] If the Commission adopts one of the range options, that option should be uniformly applied to all accounts.

VI. The Commission must deal with the existing reserve deficiency in the technology accounts as part of simplification.

If the Commission's simplification initiative is to have significant long term benefits for carriers and their customers, the Commission must deal with the existing reserve deficiencies in the technology accounts. As demonstrated above, BellSouth currently has a depreciation reserve deficiency of more than $1.5 Billion in the three Metallic Cable accounts and the Circuit-Other account, based on BellSouth's forecasted lives. This quantification does not take into specific account the loss in actual economic value that will be brought about by the acceleration in competition growing out of the Commission's initiatives in

[35]The quantification of savings resulting from the various options is contained in the Comments of the Untied States Telephone Association, which has compiled individual company data to provide composite savings for the LEC industry.

Dockets 91-141 and 91-213.

A. BellSouth's existing reserve deficiency justifies a reserve deficiency amortization.

The inadequate state of the depreciation reserve in BellSouth's technology accounts is a direct result of the Commission's actions in prescribing longer lives for these accounts than requested by BellSouth. The Commission's overriding emphasis on historical mortality data under the existing process has obscured the prospects of technological obsolescence in these accounts. Furthermore, under traditional rate of return regulation and current price cap regulation, customers have not been charged rates that are sufficient to accurately recover the investment in these accounts. As a result, BellSouth believes that it is legally entitled to a reserve deficiency amortization, including exogenous treatment under price cap regulation.[36]

B. Adoption of the PCCO could avoid the necessity of reserve deficiency amortizations.

An alternative to a reserve deficiency amortization would be for the Commission to adopt promptly the PCCO. If this option were adopted, as proposed herein, BellSouth believes that it could, consistent with GAAP, recover the existing reserve deficiency over the remaining life of the

[36] See Property Depreciation, 83 FCC 2d 267, 276-277 (1980), citing Democratic Central Committee v. Washington Metropolitan Area Transit Committee, 48 F.2d 786 (D.C. Cir. 1973).

assets in these accounts.[37] This is essentially the treatment that the Commission has accorded AT&T. AT&T's currently prescribed MR depreciation rate of 13.8 percent is almost twice BellSouth's composite MR depreciation rate of 7.0 percent. See page 18, above.

If the Commission does not adopt the PCCO and a price cap LEC is required to seek a reserve deficiency amortization because of inadequate Commission-prescribed depreciation rates, such amortization must be afforded exogenous treatment.

VII. <u>The proposed treatment of net salvage is unnecessary if the PCCO or range options are adopted in this proceeding</u>.

In paragraph 43 of the NPRM, the Commission seeks comment on whether it should, independent of the other four simplification options, change its approach to salvage and not consider it in the depreciation process. The carriers would remove salvage from the depreciation process and book the cost of removal and salvage as current period charges and credits.

BellSouth believes that the present treatment accords with GAAP, and would not be burdensome under the PCCO. It

[37] Existing GAAP favors shortening depreciable lives when possible rather than writing asset values down. See <u>APB Statement No. 4</u> (1970), Section 183, paragraph S-5c, <u>Obsolescence</u>: "Reductions in the ability of productive facilities caused by obsolescence due to technological, economic, or other change are usually recognized over the remaining productive lives of the assets. If the productive facilities have become worthless the entire loss is recognized."

is only where vintage level data is examined in detail, and where adjustments go back as far as ten years, that the current process becomes burdensome. Adoption of the PCCO or either range option considered in the NPRM will make such detailed examination unnecessary.

CONCLUSION

This docket provides the Commission with an opportunity to greatly simplify and improve its regulation of the depreciation process, while at the same time providing carriers with the depreciation flexibility required in a technologically and competitively volatile environment. The current process simply is not working. The choice of doing nothing is far more perilous to carriers, their customers, and the economy than any perceived risk of simplifying and reforming the depreciation process. The adoption of the Price Cap Carrier Option in this proceeding will greatly reduce the economic inefficiency and cost of the current regulatory process, while at the same time providing customers with adequate safeguards against manipulation of the depreciation process. In a time of tightening budgets